

# Business Valuation – Impact of Covid-19

Thursday 22<sup>nd</sup> April  
Presented by Vincent Harney



# Business Valuation

Vince Harney MRICS, MSCSI, FCA, CTA, BFP , CEO Anisorian 22 April 2021

# Overview

The Covid-19 pandemic and resulting lockdowns across the world have significantly impacted how business valuation is carried out in these uncertain times. This session will look at

- Global economic impact of covid-19
- Valuation risks factors including volatility in global markets and uncertainty of business cash flow
- Valuation considerations
- Should any valuation adjustments be applied?

# Business Valuation Refresher

Methodologies of Valuing a Business  
IVS 200

- **Multiples**

Application of Multiples to EBITDA (Operating Asset- Ignores other Assets in Business)

- **Discounted Cash Flow (DCF)**

Common Valuation technique discounting future cashflows to Present day Values using a discount rate

- **Fair Value Assessment (FVA)**

More an Accounting consideration

- **Market Approach (IVS 105)**

Stocks, Prior Transaction ,Acquisitions, Market similar companies

- **Income Approach (IVS 105)**

Capitalised Income or Discounted Cash flow

- **Cost Approach (IVS 105)**

Appropriate for example Start Ups

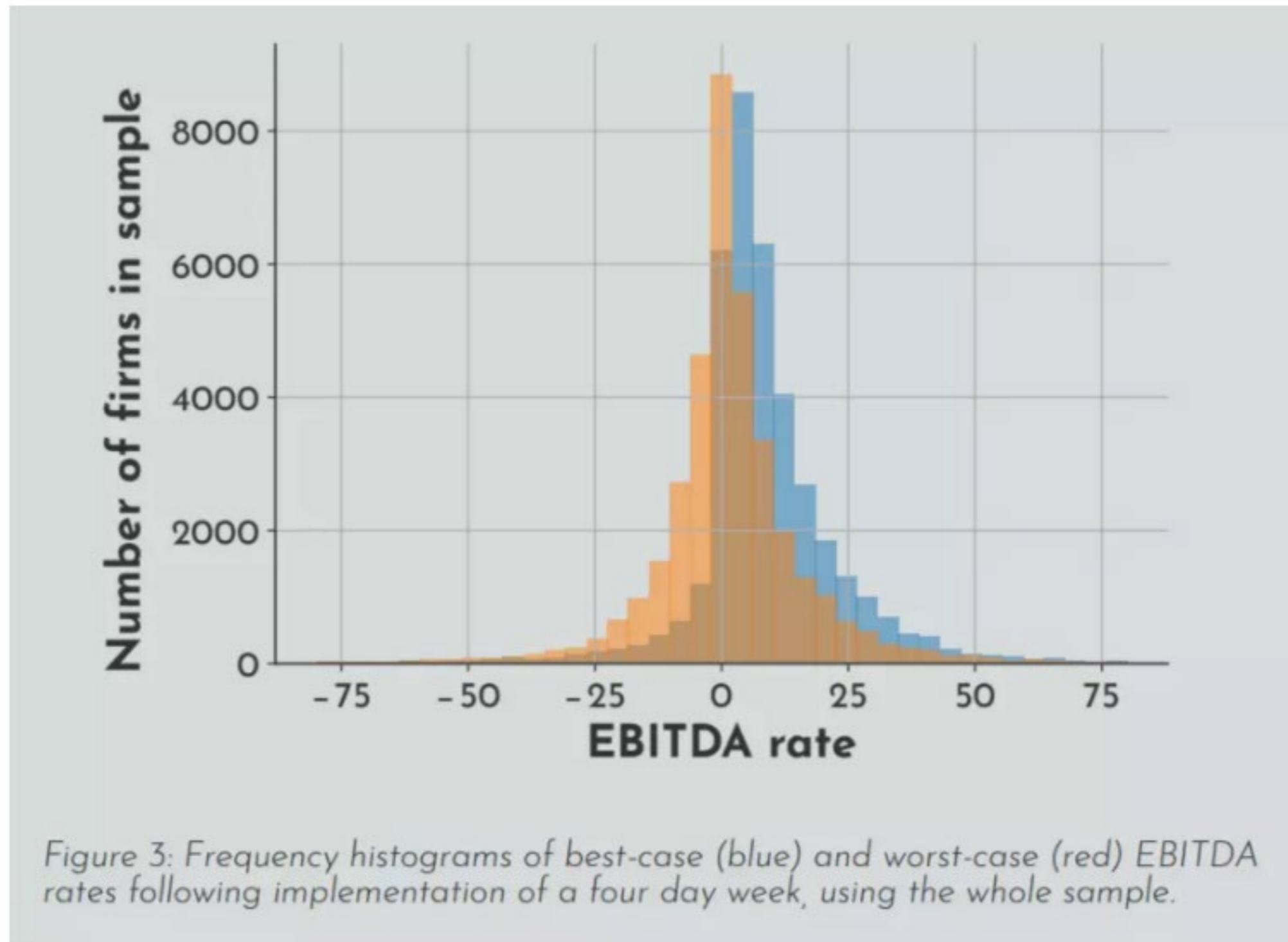


# Effect Of Pandemic – Globally – Overview

Impact Factors- Economic Macro Micro

- Collapse of Consumer Confidence
- Depressed Economic activity – suppressed GDP
- Decrease of Capital raises by Corporates
- Cancellation /Suspension of Dividends
- Potential Unemployment
- Redefinition of Retail and Hospitality Sectors
- Change in Consumer consumption and demand
- Change in US Election- positive?
- Potential ongoing Brexit issues ?
- Redefinition of work methodology and Use of Offices

# Effect of Pandemic – 4 day Week??



Under a worst-case scenario, a four-day week would be affordable for most businesses.

Image: Autonomy

# World Economic Forum – Covid and Climate Change

## Top Risks

by likelihood

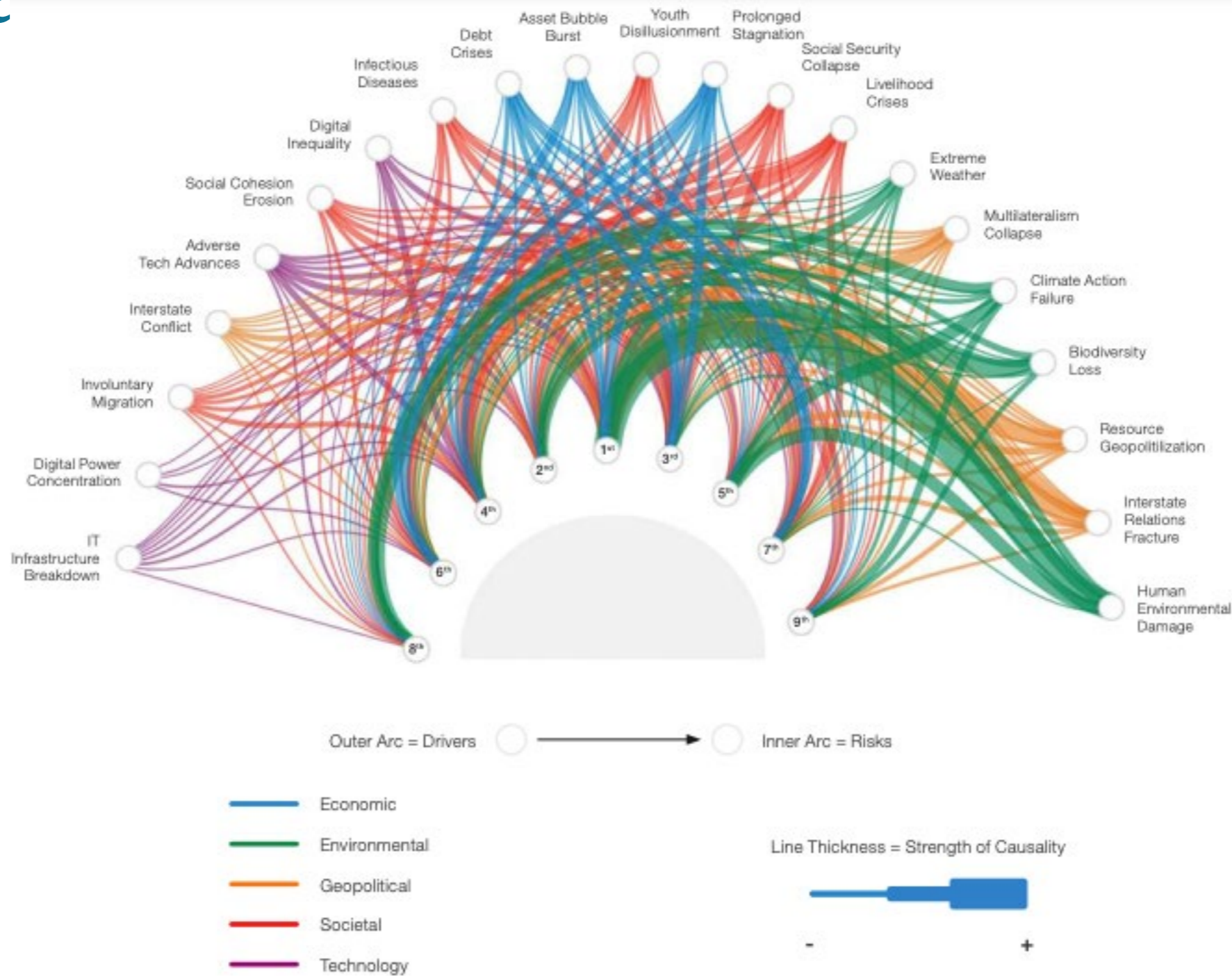
- 1 Extreme weather
- 2 Climate action failure
- 3 Human environmental damage
- 4 Infectious diseases
- 5 Biodiversity loss
- 6 Digital power concentration
- 7 Digital inequality
- 8 Interstate relations fracture
- 9 Cybersecurity failure
- 10 Livelihood crises

## Top Risks

by impact

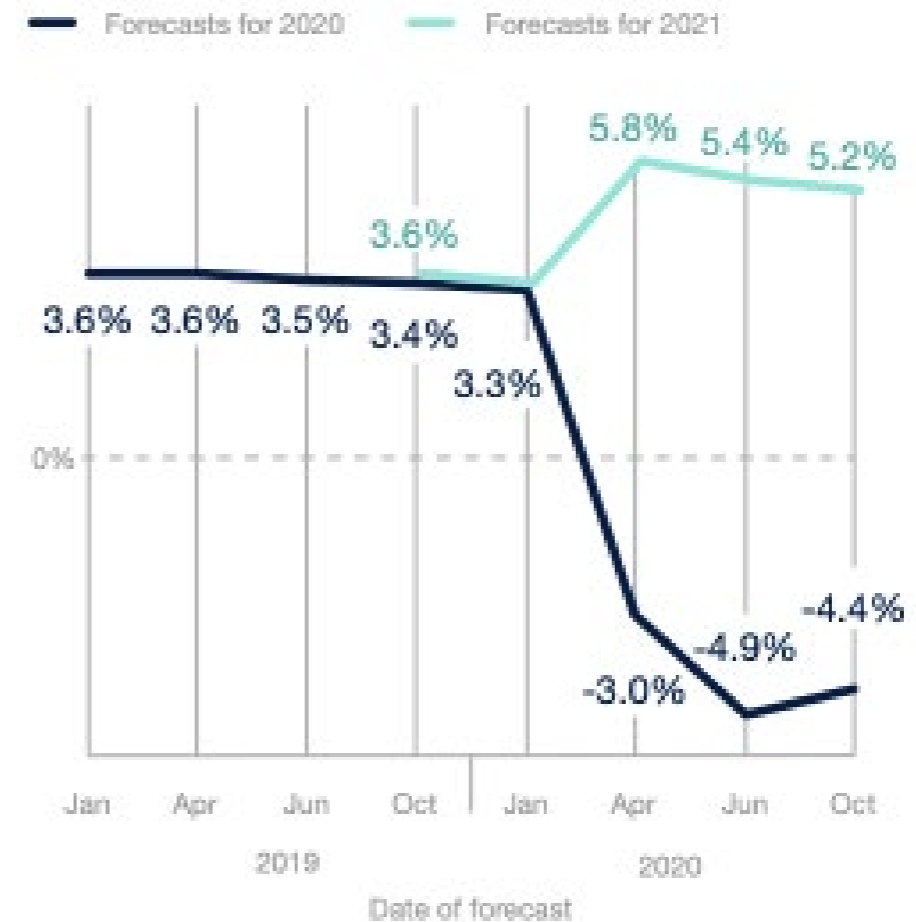
- 1 Infectious diseases
- 2 Climate action failure
- 3 Weapons of mass destruction
- 4 Biodiversity loss
- 5 Natural resource crises
- 6 Human environmental damage
- 7 Livelihood crises
- 8 Extreme weather
- 9 Debt crises
- 10 IT infrastructure breakdown

# World Economic Forum – What Drives Global Risk



# WEF- IMF World Output Projections– 2021

## IMF World Output Projections



Source: IMF. 2019 and 2020. World Economic Outlooks and quarterly updates. <https://www.imf.org/en/Publications/WEO>

# WEF– Peak Impact of COVID-19 on Key Macro Economic Indicators– G7

Economy	Annual GDP Growth		Unemployment	Business Confidence
	Q2-2020	Q3-2020	(percentage point change Q2-2020 vs Q1-2020)	(percent change first half of 2020)
China	3.2%	4.9%	+0.1	1.6%
France	-18.9%	-3.9%	-0.7	-3.3%
Germany	-11.2%	-4.0%	+0.6	-1.6%
India	-23.5%	-7.5%	N/A	1.2%
Japan	-10.3%	-5.7%	+0.4	-1.6%
United Kingdom	-21.5%	-9.6%	-0.1	-3.0%
United States	-9.0%	-2.9%	+9.2	-0.6%

Sources: OECD Data, "Business confidence index (BCI)", <https://data.oecd.org/leadind/business-confidence-index-bci.htm#indicator-chart>, accessed 20 December 2020; Ministry of Human Resources and Social Security of the People's Republic of China, Human Resources and Social Security Quarterly Data, "First quarter of 2020", <http://www.mohrss.gov.cn/SYrlzyhshbzb/zwgk/szrs/tjsj/202004/W020200423600503595588.pdf> and "First half of 2020", <http://www.mohrss.gov.cn/SYrlzyhshbzb/zwgk/szrs/tjsj/202007/W020200724600005492242.pdf>, accessed 20 December 2020.

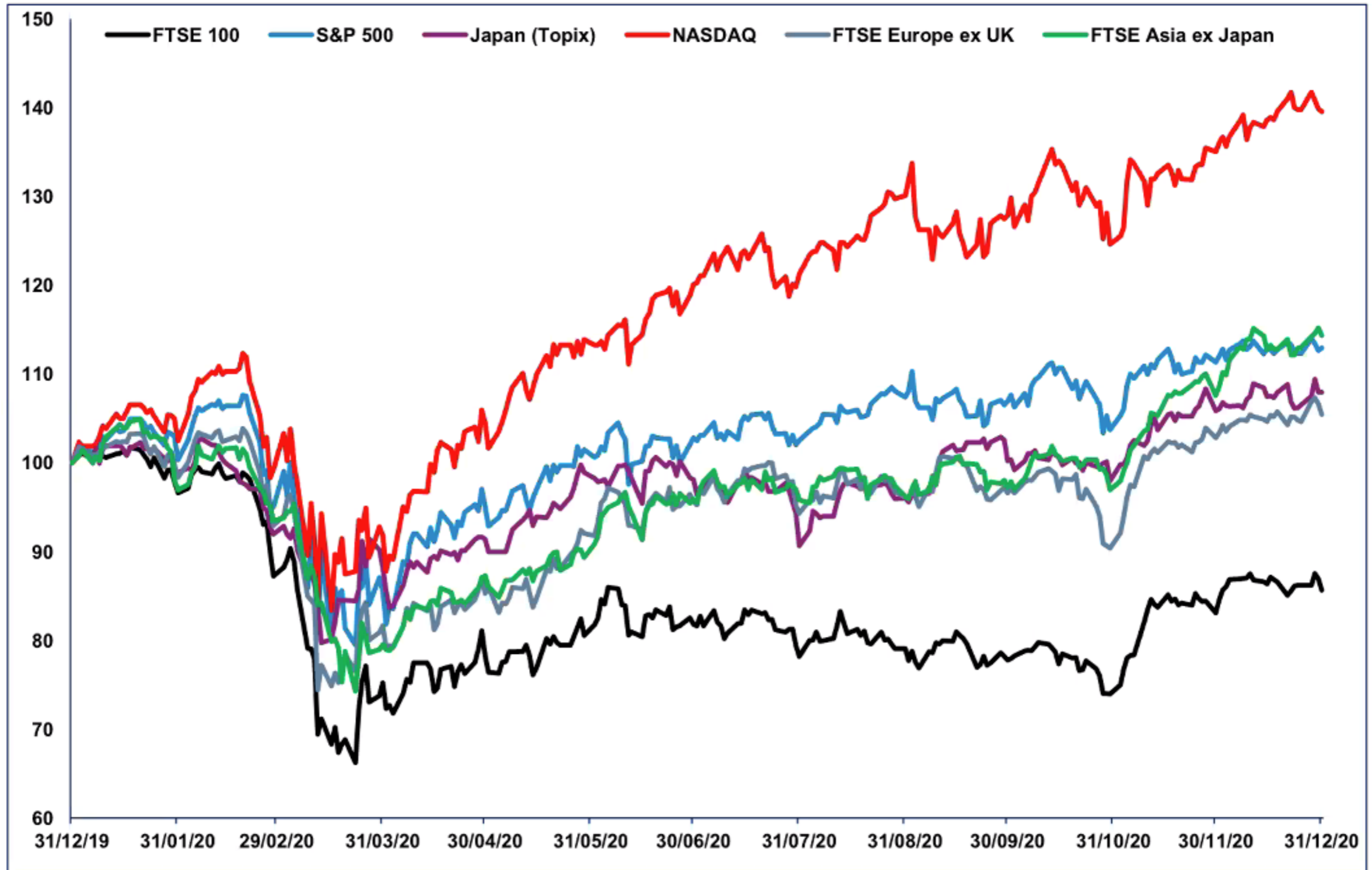
Note: Change in Business Confidence between December 2019 and May 2020, when the indicator registered its lowest data point for OECD countries in aggregate.

# Effect Of Pandemic – Globally-Positives

Impact Factors- Economic Macro Micro

- Governments unprecedented support for Businesses and Individuals  
Furlough Schemes, Supports, continuing Grants
- Central Bank Support to Governments
- Bank Support To Businesses
- Bank Support to Individuals – Mortgage Hols etc
- Low Inflation Rates
- Low Interest Rates
- Investment potential explosion of activity
- Current advantages for Cash rich Investors to pick up discounted businesses/ projects etc

# Global Markets Performance – 12 Months



# Valuation Risks factors

## Volatility in the Global Markets

- Latter Quarters of 2020 experienced significant market convulsions and increased volatility particularly over the past couple of months,
- This **will** impact valuations in the form of **higher discount rates**. These rates will likely rise along with debt margins and betas as investors become more risk averse.

# Valuation Risks factors

## Uncertainty of Business Specific Cash Flows

- **Forecasting** On a company level, the uncertainty surrounding the true economic impact of Covid-19 has resulted in corresponding difficulties with business plan forecasting. Forecast estimates would usually take the impact of the crisis into account.
- However, without reliable economic forecasts available, companies will need to look to other company-specific risks so as to produce a reasonable business forecast.

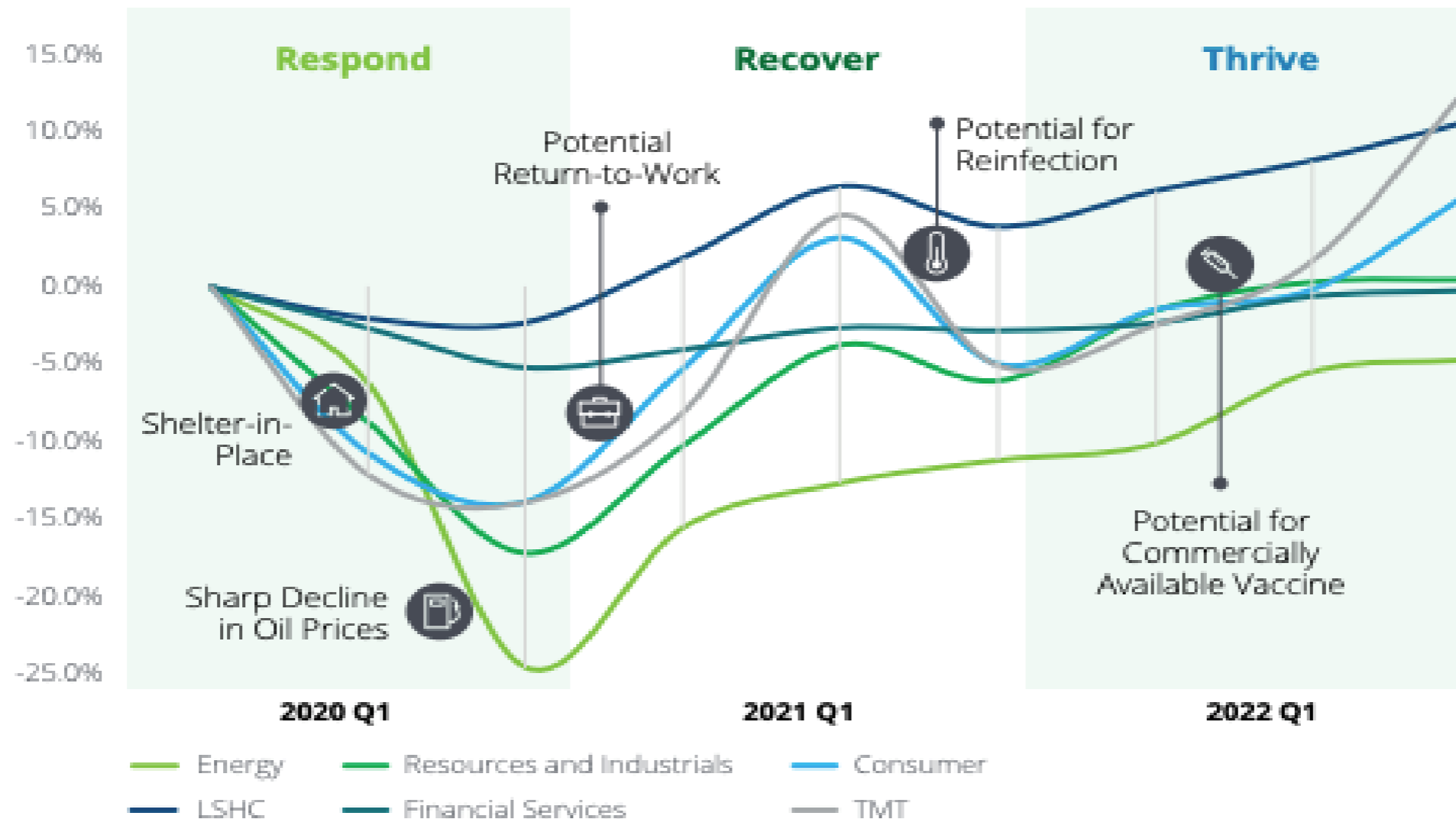
# Valuation Risks factors

## Financial Risk Factors

- **Loan Defaults** The ongoing operational and economic uncertainties will likely lead to an increase in counterparty risk, and we may see a number of companies defaulting on their outstanding obligations.
- Increase the risk of investing through counterparties that either operate in high risk industries or have low credit ratings.
- Many companies are reporting a rise in liquidity risk as they find themselves unable to deliver on short term obligations.
- Banking institutions have announced various measures aimed at maintaining a certain level of liquidity in the market. These measures are outlined in this report.

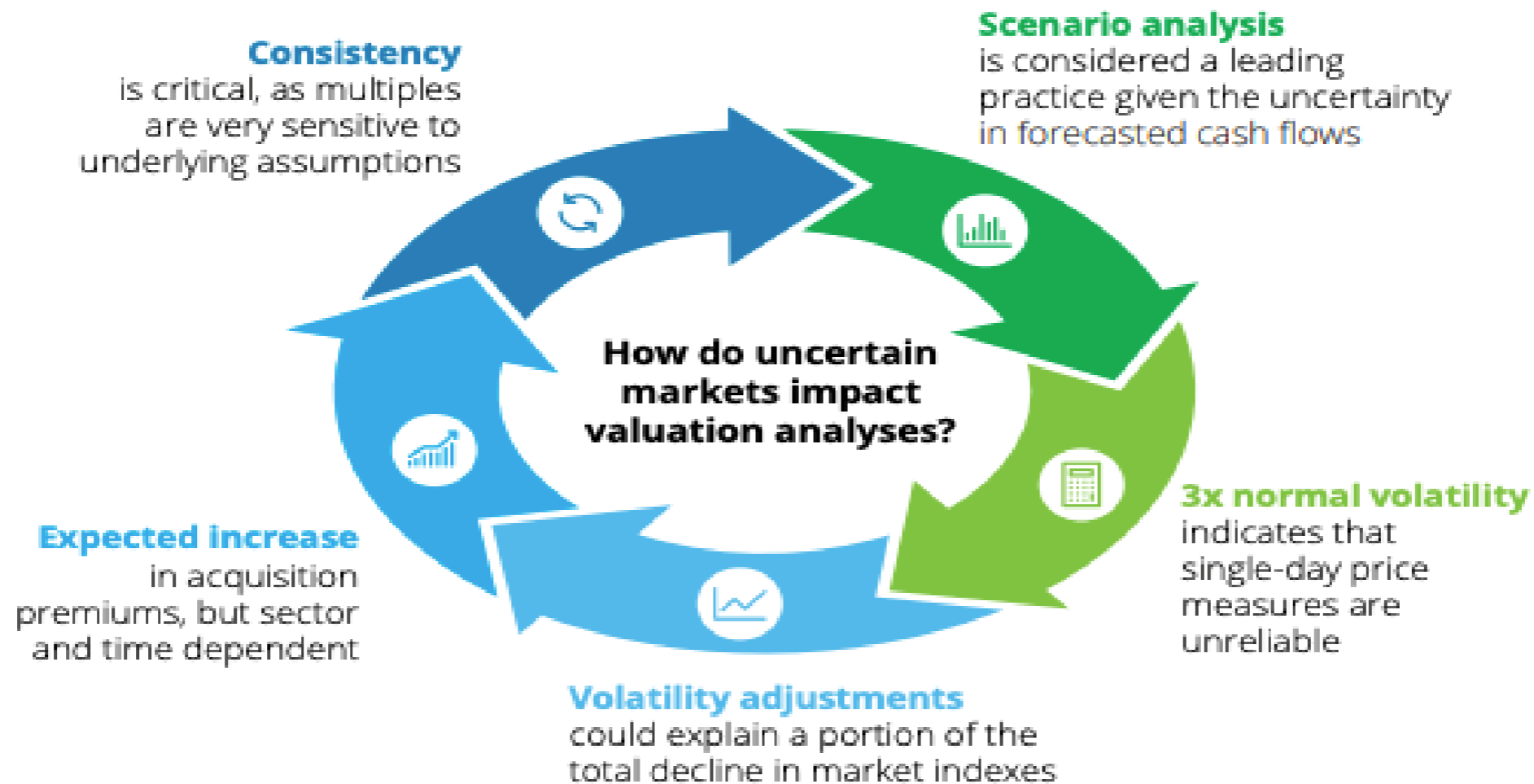
Due to these heightened risk factors, there will be a rise in debt covenant breaches, insolvencies and asset impairments in the short- and medium-term.

# Price versus Intrinsic Value



Source: S&P Capital IQ. Based on S&P 500 analyst EPS growth percentage forecasts by sector; coupled with example milestones that may explain trends

# How do uncertain Markets impact Valuation Analyses?



# Valuation considerations

## IVSC – International Valuation Standards

The IVSC issue the IVS and unlike RICS Red Book cover Business Valuations:

### Core Considerations

- Market Value of Business
- Fair Value of Business
- Cash on Cash
- Future Assessment of Businesses.
- Multiples.
- DCF Approach (incl EIRR, NPV.)

.

# Valuation considerations – Uncertainty at Times of Market Unrest

IVSC – International Valuation Standards



March 2020

## Dealing with valuation uncertainty at times of market unrest

This letter is issued by the IVSC's technical boards and is intended as a helpful summary of key parts of the International Valuation Standards (IVS), which might be of particular relevance during periods of market uncertainty.

This paper is not a standard. Valuers should refer to the latest version of IVS when carrying out a valuation. IVS can be accessed online at: [www.ivsonline.org](http://www.ivsonline.org)

# Valuation considerations – Measuring Valuation Uncertainty

IVSC – International Valuation Standards

- Quantification easier for some Businesses/Assets than Others
- Scenario and Sensitivity Analyses should be core in the Model
- Difficult to apply to Non Financial Asset due to lower Volumes
- Monte Carlo Simulations – Multiple iterations

# Valuation considerations – Measuring Valuation Uncertainty

RICS – Beyond COVID 19



**Beyond COVID-19:**

Valuation approaches and evidence  
during the COVID-19 health crisis



# Valuation considerations – Measuring Valuation Uncertainty

RICS Approach- Property Yes but also same Principle for Business

- Discounted Cash Flow CORE
- Market Value and Income Approach with Sensitivities
- Material Valuation Uncertainty
- Market Comparables- is there a Market there?
- Be Aware of Discount Rate structure
- Be aware of All Risks Yields

## 7 The income approach to valuation during COVID-19 (including with reference to individual trade related properties)

For certain assets and markets the income approach to valuation is the most suitable. The current COVID-19 health crisis has caused uncertainty around future income streams and therefore particular professional considerations around the use of the income approach. Income uncertainty might be a short-term issue or, where there are predicted knock-on behavioural, regulatory or economic effects, a longer-term consideration. The more unknown these effects are and the longer the expected duration of uncertainty, the greater challenge there is with the use of the income approach.

**The use of the income approach is only appropriate where the valuer has the experience and competence to be able to apply it to the class of asset being valued within the relevant market.** Where the valuer is not familiar with the income approach and it is the principle approach relevant to the market for the asset being valued, they should consider whether they are able to undertake the valuation.

# Valuation considerations – Measuring Valuation Uncertainty

## General Valuation Considerations

- Greater uncertainty results in higher risk, which in turn justifies the demand for greater returns. This will ultimately result in lower asset values.
- The short-, medium- and long-term impacts of the crisis, whether they be macro-economic or business-specific, will need to be taken into consideration. The market disruption observed today may be temporary, and the adjustments we make could potentially overstate or understate the crisis' impact on the company's valuation.
- Fair value is based on what is known and knowable at the measurement date. The assumptions taken into consideration today may no longer be applicable tomorrow, which means that the procedures and rationale for any valuations you perform should be documented in full.
- Assessing the going concern status of companies will also be key, so valuations should focus on companies' short-term cash flows and liquidity needs. Currently Core in Audits by ICAEW /CCAB /CAI/IIA

# Valuation considerations – Measuring Valuation Uncertainty

## Other Considerations

- **Liquidity Needs** – for Example Breaches of Debt Covenants- Financing Working Capital, impact of extended reduced Cash
- Credit Risk Assessment
- Trading Risks beyond COVID – Brexit for example

# Should any valuation adjustments be applied?

- IVS 103 SIGNIFICANT UNCERTAINTY DISCLOSURE
- If Quantifiable – Yes!!

“Managers and investors alike must understand that accounting numbers are the beginning, not the end, of business valuation.”

Warren Buffett





# Q & A's

[www.anisorian.com](http://www.anisorian.com)